

**Artesian Water Company, Inc.
(A Wholly Owned Subsidiary of
Artesian Resources Corporation)**

Financial Statements

Years Ended December 31, 2011 and 2010

The report accompanying these financial statements was issued by
BDO USA, LLP, a Delaware limited liability partnership and the U.S. member of BDO
International Limited, a UK company limited by guarantee.

BDO.

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(A Wholly Owned Subsidiary of
Artesian Resources Corporation)**

Financial Statements

Years Ended December 31, 2011 and 2010

Artesian Water Company, Inc.

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Independent Auditors' Report

To the Board of Directors and Stockholder
Artesian Water Company, Inc.
Newark, Delaware

We have audited the accompanying balance sheets of Artesian Water Company, Inc. ("the Company") as of December 31, 2011 and 2010 and the related statements of operations and retained earnings, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Artesian Water Company, Inc. at December 31, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

BDO USA, LLP

Bethesda, Maryland
April 19, 2012

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Artesian Water Company, Inc.

Balance Sheets (In Thousands)

December 31,	2011	2010
ASSETS		
Utility Plant, at original cost (less accumulated depreciation 2011-\$74,849; 2010-\$67,657)	\$ 308,984	\$ 305,208
Current Assets		
Cash and cash equivalents	4	4
Accounts receivable (less allowance for doubtful accounts 2011-\$121; 2010-\$124)	3,306	3,109
Loan receivable from parent	10,988	-
Receivables-related party	-	258
Unbilled operating revenues	3,636	3,614
Materials and supplies - at cost on first-in first-out basis	1,472	1,243
Prepaid property taxes	1,287	1,257
Prepaid expenses and other	1,122	1,596
	21,815	11,081
Other Assets		
Non-utility property (less accumulated depreciation 2011-\$74; 2010-\$65)	183	193
Other deferred assets	4,560	4,405
	4,743	4,598
Regulatory Assets	1,436	1,242
	\$ 336,978	\$ 322,129
Liabilities and Capital		
Capitalization		
Common stock-\$1 par value (1,000 shares authorized, issued and outstanding)	\$ 1	\$ 1
Additional paid-in-capital	79,257	63,616
Retained earnings	21,641	20,912
Total stockholder's equity	100,899	84,529
Long-term debt, net of current portion	106,539	104,481
	207,438	189,010
Commitments and Contingencies		
Current Liabilities		
Lines of credit	---	5,588
Current portion of long-term debt	1,137	964
Accounts payable	2,674	3,297
Accrued expenses	2,250	1,978
Overdraft payable	269	650
Loan payable to parent	-	1,655
Payables - related party	234	-
Deferred income taxes	817	531
Accrued interest	1,207	1,148
Customer deposits	942	805
Other	1,549	1,599
	11,079	18,215
Deferred Credits and Other Liabilities		
Net advances for construction	14,026	15,978
Postretirement benefit obligation	456	524
Deferred investment tax credits	643	664
Deferred income taxes	41,262	36,981
	56,387	54,147
Net Contributions In Aid of Construction	62,074	60,757
	\$ 336,978	\$ 322,129

See accompanying summary of significant accounting policies and notes to financial statements.

Artesian Water Company, Inc.

Statements of Operations and Retained Earnings (In Thousands)

<i>Year Ended December 31,</i>	2011	2010
Operating Revenues		
Water sales	\$ 57,003	\$ 56,608
Other	1,642	1,439
	58,645	58,047
Operating Expenses		
Operation and maintenance expenses	30,317	29,469
Depreciation and amortization	6,886	6,567
Taxes		
State and federal income taxes		
Current	-	823
Deferred	4,631	4,038
Property and other	3,536	3,478
	45,370	44,375
Operating Income	13,275	13,672
Other Income, Net		
Allowance for funds used during construction (AFUDC)	112	136
Miscellaneous	487	465
Income Before Interest Charges	13,874	14,273
Interest Charges		
Long-term debt	6,786	6,743
Short-term debt	66	167
Amortization of debt expense	117	117
Other	5	2
	6,974	7,029
Net Income	6,900	7,244
Retained Earnings, beginning of year	20,912	19,177
Less: dividends to parent company	6,171	5,509
Retained Earnings, end of year	\$ 21,641	\$ 20,912

See accompanying summary of significant accounting policies and notes to financial statements.

Artesian Water Company, Inc.

Statements of Cash Flows (In Thousands)

Year Ended December 31,	2011	2010
Cash Flows From Operating Activities		
Net income	\$ 6,900	\$ 7,244
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,886	6,567
Deferred income taxes, net	4,546	3,385
AFUDC, equity portion	(66)	(80)
Changes in assets and liabilities:		
Accounts receivable, net of allowance for doubtful accounts	61	5,610
Unbilled operating revenues	(22)	(96)
Materials and supplies	(229)	(25)
Regulatory assets	(194)	371
Postretirement benefit obligation	(68)	(213)
Other deferred assets	(247)	(187)
Prepaid property taxes	(30)	(37)
Prepaid expenses and other	474	(655)
Accounts payable	(389)	54
Accrued expenses	272	1,383
Accrued interest	59	(180)
Customer deposits and other, net	87	423
Net cash provided by operating activities	18,040	23,564
Cash Flows From Investing Activities		
Capital expenditures (net of AFUDC, equity portion)	(11,702)	(13,136)
Proceeds from sales of assets	55	61
Net cash used in investing activities	(11,647)	(13,075)
Cash Flows From Financing Activities		
Net (repayments) under lines of credit agreements	(5,588)	(7,341)
Change in deferred debt issuance costs	91	36
Net (repayments) borrowings from parent company	(1,655)	1,655
Net issuance of loan to parent company	(10,988)	-
Net proceeds from issuance of common stock	15,641	-
Principal repayments of long-term debt	(964)	(369)
Issuance of long-term debt	3,195	-
(Decrease) in overdraft payable	(381)	(366)
Net advances and contributions in aid of construction	427	1,214
Dividends to parent company	(6,171)	(5,509)
Net cash provided by (used in) financing activities	(6,393)	(10,680)
Net increase(decrease) in cash and cash equivalents	-	(191)
Cash and cash equivalents, Beginning of year	4	195
Cash and cash equivalents, End of year	\$ 4	\$ 4
Supplemental Disclosures of Cash Flow Information:		
Utility plant received as construction advances and contributions	\$ 154	\$ 47
Supplemental Disclosures of Cash Flow Information:		
Interest paid	\$ 6,914	\$ 7,209

See accompanying summary of significant accounting policies and notes to financial statements.

Artesian Water Company, Inc.

Summary of Significant Accounting Policies

Basis of Accounting

Artesian Water Company, Inc., Artesian Water or the Company, is a wholly-owned subsidiary of Artesian Resources Corporation, or Artesian Resources. The Company provides water utility service to customers within its established service areas in Delaware, pursuant to rates filed with and approved by the Delaware Public Service Commission (the "DEPSC"). As of December 31, 2011, the Company served approximately 78,600 customers. The accounting records of the Company are maintained in accordance with the uniform system of accounts as prescribed by the DEPSC. The Company follows the provisions of the Financial Accounting Standards Board Accounting Standards Codification, or FASB ASC, Topic 980, which provides guidance for companies in regulated industries.

Reclassification

Certain accounts in the prior year financial statements have been reclassified for comparative purposes to conform with the presentation in the current year financial statements. These reclassifications had no effect on net income or stockholder's equity.

Utility Plant

All additions to plant are recorded at cost. Cost includes direct labor, materials, and indirect charges for such items as transportation, supervision, pension, and other fringe benefits related to employees engaged in construction activities. When depreciable units of utility plant are retired, the cost of retired property, together with any cost associated with retirement and less any salvage value or proceeds received, is charged to accumulated depreciation. In accordance with a DEPSC rate order issued on January 31, 2012, effective January 1, 2012, any cost associated with retirement less any salvage value or proceeds received will be charged to a regulated retirement liability. This new approach will result in an approximately \$1.2 million reclassification of utility plant to deferred credits and other liabilities on our Balance Sheet in our fiscal year 2012. Maintenance, repairs, and replacement of minor items of plant are charged to expense as incurred.

In accordance with a rate order issued by the DEPSC, Artesian Water accrues an Allowance for Funds Used During Construction or AFUDC. AFUDC, which represents the cost of funds devoted to construction projects through the date the project is placed in service, is capitalized as part of construction work in progress. The rate used for the AFUDC calculation is based on Artesian Water's weighted average cost of debt and the rate of return on equity authorized by the DEPSC. The rate used to capitalize AFUDC in 2011 and 2010 was 8.2% and 7.9%, respectively.

Artesian Water Company, Inc.

Summary of Significant Accounting Policies

Utility plant at December 31, comprised of:

<i>In thousands</i>	<i>Estimated Useful Life In Years</i>	<i>December 31, 2011</i>	<i>2010</i>
Utility plant at original cost			
Utility plant in service			
Intangible plant	-	\$ 140	\$ 140
Source of supply plant	45-85	16,458	15,938
Pumping and water treatment plant	35-62	56,435	54,731
Transmission and distribution plant			
Mains	81	180,724	176,927
Services	39	30,406	29,702
Storage tanks	76	21,131	20,938
Meters	26	19,699	17,133
Hydrants	60	10,056	9,630
General plant	3-31	44,540	42,389
Property held for future use	-	1,299	1,876
Construction work in progress	-	2,945	3,461
		383,833	372,865
Less - accumulated depreciation		74,849	67,657
		\$ 308,984	\$ 305,208

Depreciation and Amortization

For financial reporting purposes, depreciation is recorded using the straight-line method at rates based on estimated economic useful lives, which range from 3 to 85 years. Composite depreciation rates for water utility plant were 2.22% for 2011 and 2.18% for 2010. In a rate order issued by the DEPSC, the Company was directed effective January 1, 1998 to begin using revised depreciation rates for utility plant. In rate orders issued by the DEPSC, Artesian Water was directed effective May 28, 1991 and August 25, 1992 to offset depreciation recorded on utility plant by depreciation on utility property funded by Contributions in Aid of Construction, or CIAC, and Advances for Construction, or Advances, respectively. This reduction in depreciation expense is also applied to outstanding CIAC and Advances.

Regulatory Assets

FASB ASC Topic 980 stipulates generally accepted accounting principles for companies whose rates are established by or are subject to approval by a third-party regulatory agency. Certain expenses are recoverable through rates charged to our customers, without a return on investment, and are deferred and amortized during future periods using various methods as permitted by the DEPSC. Depreciation and salary study expenses are amortized on a straight-line basis over a period of five years and two years for all other expenses related to Delaware rate proceedings and applications to increase rates. Artesian Water recognizes an offsetting regulatory asset with respect to its postretirement benefit obligation (see Note 5 to our Financial Statements for a description of the Company's Postretirement Benefit Plan). The deferred income taxes will be amortized over future years as the tax effects of temporary differences previously flowed through to the customers

Artesian Water Company, Inc.

Summary of Significant Accounting Policies

reverse.

Regulatory assets at December 31, net of amortization, comprise:

<i>In thousands</i>	2011	2010
Postretirement benefit obligation	\$ 567	\$ 637
Deferred income taxes	506	521
Expense of rate and regulatory proceedings	363	84
	\$ 1,436	\$ 1,242

Impairment or Disposal of Long-Lived Assets

Our long-lived assets consist primarily of utility plant in service and regulatory assets. A review of our long-lived assets is performed in accordance with the requirements of FASB ASC Topic 360. In addition, the regulatory assets are reviewed for the continued application of FASB ASC Topic 360. The review determines whether there have been changes in circumstances or events that have occurred requiring adjustments to the carrying value of these assets. FASB ASC Topic 360 stipulates that adjustments to the carrying value of these assets would be made in instances where the inclusion in the rate-making process is unlikely.

Other Deferred Assets

Debt issuance costs are amortized over the term of the related debt, which range from 10 to 30 years. The investment in Co-Bank, which is a cooperative bank, is related to certain outstanding First Mortgage Bonds and is a required investment in the bank based on the underlying long term debt agreements.

Other deferred assets at December 31, net of amortization, comprised:

<i>In thousands</i>	2011	2010
Debt issuance cost	\$ 2,228	\$ 2,300
Investment in Co-Bank	2,294	2,067
Other	38	38
	\$ 4,560	\$ 4,405

Advances for Construction

Water mains, services and hydrants, or cash advances to reimburse Artesian Water for its costs to construct water mains, services and hydrants are contributed to Artesian Water by customers, real estate developers and builders in order to extend water service to their properties. The value of these contributions is recorded as Advances for Construction. Artesian Water makes refunds on these advances over a specific period of time based on operating revenues generated by the specific plant or as new customers are connected to the mains. After all refunds are made within

Artesian Water Company, Inc.

Summary of Significant Accounting Policies

the contract period, any remaining balance is transferred to CIAC.

Contributions in Aid of Construction

CIAC includes the non-refundable portion of advances for construction and direct contributions of water mains, services and hydrants, or cash to reimburse for costs to construct water mains, services and hydrants.

Income Taxes

The Company is included in the consolidated tax returns of its parent, Artesian Resources Corporation. However, for financial statement purposes, the Company calculates its tax provision on a separate return basis.

Deferred income taxes are provided in accordance with FASB ASC Topic 740 on all differences between the tax basis of assets and liabilities and the amounts at which they are carried in the consolidated financial statements based on the enacted tax rates expected to be in effect when such temporary differences are expected to reverse. Under FASB ASC Topic 740, the Company analyzed its various tax positions and determined that no further entry, recognition or derecognition was required. The Company would recognize, if applicable, interest accrued and penalties related to unrecognized tax benefits in interest expense and in accordance with the regulations of the jurisdictions involved.

The Tax Reform Act of 1986 mandated that Advances and CIAC received subsequent to December 31, 1986, generally are taxable income. The 1996 Tax Act provided an exclusion from taxable income for CIAC and Advances received after June 12, 1996 by our utilities except for certain contributions for large services that are not included in rate base for rate-making purposes.

Investment tax credits were deferred through 1986 and are recognized as a reduction of deferred income tax expense over the estimated economic useful lives of the related assets.

Revenue Recognition and Unbilled Revenues

Water service revenue for financial statement purposes includes amounts billed to customers on a quarterly or monthly cycle basis, depending on class of customer, and unbilled amounts based upon estimated usage from the date of the last meter reading to the end of the accounting period. As actual usage amounts are received, adjustments are made to the unbilled estimates in the next billing cycle based on the actual results.

Artesian Water Company, Inc.

Summary of Significant Accounting Policies

Accounts Receivables

Accounts receivable are recorded at the invoiced amounts. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in our existing accounts receivable. The Company reviews the allowance for doubtful accounts on a quarterly basis. Account balances are written off against the allowance when it is probable the receivable will not be recovered. The allowance for doubtful accounts was \$121,000 at December 31, 2011 and \$124,000 at December 31, 2010. The corresponding expense for the year ended December 31, 2011 and 2010 was \$253,000 and \$292,000, respectively. The following table summarizes the changes in the Company's accounts receivable balance:

Receivables at December 31, comprised:

<i>In thousands</i>	2011	2010
Customer accounts receivable - water	\$ 3,353	\$ 3,143
Receivables-Intercompany	-	258
Other	74	90
	3,427	3,491
Less allowance for doubtful accounts	121	124
Net accounts receivable	\$ 3,306	\$ 3,367

The activities in the allowance for doubtful accounts are as follows:

Allowances at December 31, comprised:

<i>In thousands</i>	2011	2010
Beginning balance	\$ 124	\$ 97
Allowance adjustments	253	292
Recoveries	108	68
Write off of uncollectible accounts	(364)	(333)
Ending balance	\$ 121	\$ 124

Cash and Cash Equivalents

For purposes of the Statement of Cash Flows, the Company considers all temporary cash investments with an original maturity of three months or less to be cash equivalents. The Company utilizes its bank's zero balance account disbursement service to reduce the use of their lines of credit by funding checks as they are presented to the bank for payment rather than at issuance. If the checks currently outstanding, but not yet funded, exceed the cash balance on our books, the net liability is recorded as a current liability on the balance sheet in the Overdraft Payable account.

Artesian Water Company, Inc.

Summary of Significant Accounting Policies

Use of Estimates in the Preparation of the Financial Statements

The financial statements were prepared in conformity with generally accepted accounting principles in the U.S., which require management to make estimates about the reported amounts of assets and liabilities including unbilled revenues, reserve for a portion of revenues received under temporary rates and regulatory asset recovery and contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from management's estimate.

Subsequent Events

Management has evaluated any events or transactions occurring after the balance sheet date through April 19, 2012, the date the financial statements were available to be issued, and noted that there have been no such events or transactions which would require adjustments to or disclosure in the Company's financial statements.

Artesian Water Company, Inc.

Notes to Financial Statements

1. Fair Value of Financial Instruments

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value.

Current Assets and Liabilities

For those current assets and liabilities that are considered financial instruments, the carrying amounts approximate fair value because of the short maturity of those instruments.

Long-term Financial Liabilities

The fair value of the Company's long-term debt as of December 31, 2011 and December 31, 2010, determined by discounting their future cash flows using current market interest rates on similar instruments with comparable maturities as guided under FASB ASC 825 are shown as below:

<i>In thousands</i>	December 31,	
	2011	2010
Carrying amount	\$ 107,676	\$ 105,445
Estimated fair value	127,337	111,975

The fair value of Advances for Construction cannot be reasonably estimated due to the inability to accurately estimate the timing and amounts of future refunds expected to be paid over the life of the contracts. Refund payments are based on the water sales to new customers in the particular development constructed. The fair value of Advances for Construction would be less than the carrying amount because these financial instruments are non-interest bearing.

2. Income Taxes

The difference between the effective tax rate (2011 - 40.2%; 2010 - 40.2%) and the amount derived by multiplying income before federal and state income taxes by the statutory federal income tax rate of 34% in 2011 and 2010 is primarily attributable to state income taxes.

As of December 31, 2011, the Company has federal net operating loss carry forwards aggregating approximately \$4,403,000 which will expire if unused by 2030. As of December 31, 2011, the Company has state net operating loss carry forwards ("NOL's") aggregating approximately \$9,679,000. These NOL's will expire if unused between 2024 and 2031. At December 31, 2011, for federal income tax purposes, there were alternative minimum tax credit carry-forwards aggregating approximately \$3,688,000 resulting from the payment of alternative minimum tax in current and prior years. These alternative minimum tax credit carry-forwards may be carried forward indefinitely to offset future regular federal income taxes. The Company has not recorded a valuation allowance for these tax carry forwards, because the Company believes it is more likely than not that such benefits will be realized.

Artesian Water Company, Inc.

Notes to Financial Statements

Under FASB ASC Topic 740, an uncertain tax position represents our expected treatment of a tax position taken, or planned to be taken in the future, that has not been reflected in measuring income tax expense for financial reporting purposes. As a result of our review of Artesian's tax positions, we determined that we had no material uncertain tax positions. The Company would recognize, if applicable, interest accrued and penalties related to unrecognized tax benefits in interest expense and in accordance with the regulations of the jurisdictions involved. There were no such interest and penalty charges for the period ended December 31, 2011 or December 31, 2010. The Company remains subject to examination by state authorities for the tax years 2008 through 2011 and by federal authorities for tax years 2009 through 2011.

Deferred income taxes are comprised of the following:

<i>In thousands</i>	December 31, 2011	2010
Alternative minimum tax credit carry forwards	\$ 3,688	\$ 3,775
Bad debt allowance	89	90
Federal and state NOL's	2,053	1,834
Other	355	-
Total deferred tax assets	6,185	5,699
Deferred tax liabilities related to:		
Property, plant and equipment basis differences	(47,013)	(42,343)
Expenses of rate proceedings	(144)	(18)
Property taxes	(512)	(500)
Regulatory asset	(201)	(207)
Other	(394)	(143)
Total deferred tax liabilities	(48,264)	(43,211)
Net deferred tax liability	\$ (42,079)	\$ (37,512)

Deferred taxes, which are classified into a net current and non-current balance, are presented in the balance sheet as follows:

<i>In thousands</i>	December 31, 2011	2010
Current deferred tax liability	\$ (817)	\$ (531)
Non-current deferred tax liabilities	(41,262)	(36,981)
Net deferred tax liability	\$ (42,079)	\$ (37,512)

Artesian Water Company, Inc.

Notes to Financial Statements

The provision for income taxes consisted of the following:

<i>In thousands</i>	December 31, 2011	2010
Current tax expense:		
Federal	\$ -	\$ 823
State	-	-
	-	823
Deferred tax expense:		
Federal	3,921	3,293
State	710	745
	4,631	4,038
Total provision	\$4,631	\$ 4,861

3. Lines of Credit

Artesian Water has a \$20 million line of credit with Co-Bank, ACB that allows for the financing of operations for Artesian Water, with up to \$10 million of this line available for the operations of its affiliate Artesian Water Maryland, Inc., which is also a wholly-owned subsidiary of Artesian Resources. The interest rate for borrowings under this line is the London Interbank Offered Rate, or LIBOR, plus 1.50%. The term of this line of credit expires on January 16, 2013. Artesian Resources has a \$40 million line of credit with Citizens Bank, or Citizens, which is available to all subsidiaries of Artesian Resources. The interest rate for borrowings under this line is LIBOR plus 1.00%. This is a demand line of credit and therefore the financial institution may demand payment for any outstanding amounts at any time. The term of this line of credit expires on the earlier of May 31, 2012 or any date on which Citizens demands payment. As of December 31, 2011, Artesian Water did not have any borrowings under either of these lines of credit.

On July 20, 2011 and August 15, 2011, Artesian Resources completed the sale of 804,290 shares and 84,000 shares of its Class A Non-Voting Common Stock, respectively. The net proceeds (after deducting underwriting discounts and commissions and offering expenses) of approximately \$15.6 million were used to fund a paid-in capital contribution in the same amount to Artesian Water. Artesian Water used the paid-in capital contribution to repay short-term borrowings (including borrowings incurred under our line of credit with Citizens that is available to all the subsidiaries).

4. Long-Term Debt

As of December 31, 2011 and 2010, substantially all of Artesian Water's utility plant was pledged as security for the First Mortgage Bonds. In addition, the trust indentures relating to these First Mortgage Bonds contain covenants which limit long-term debt, including the current portion thereof, to 66 2/3% of total capitalization including the current portion of the long-term debt, and

Artesian Water Company, Inc.

Notes to Financial Statements

which, in certain circumstances, could restrict the payment of cash dividends. As of December 31, 2011, however, no dividend restrictions were imposed under these covenants.

On July 15, 2011, Artesian Water entered into a Financing Agreement, with the Delaware Drinking Water State Revolving Fund, acting by and through the Delaware Department of Health & Social Services, Division of Public Health, a public agency of Delaware, or the Department. The Company has been given a loan of approximately \$3.6 million, or the Loan, from the Delaware Safe Drinking Water Revolving Fund to finance all or a portion of the cost to replace specific water transmission mains in service areas located in New Castle County, Delaware (collectively, the "Project"). In accordance with the Financing Agreement, the Company will from time to time request funds under the Loan as it incurs costs in connection with the Project. The Company shall pay to the Department, on the principal amount drawn down and outstanding from the date drawn, interest at a rate of 1.7% per annum and an administrative fee at the rate of 1.7% per annum. As of December 31, 2011, approximately \$0.8 million was borrowed under this Loan.

<i>In thousands</i>	December 31, 2011	2010
First mortgage bonds		
Series O, 8.17%, due December 29, 2020	\$ 20,000	\$ 20,000
Series P, 6.58%, due January 31, 2018	25,000	25,000
Series Q, 4.75%, due December 1, 2043	15,400	15,400
Series R, 5.96%, due December 31, 2028	25,000	25,000
Series S, 6.73%, due December 31, 2033	13,200	13,800
	98,600	99,200
State revolving fund loans		
4.48%, due August 1, 2021	2,624	2,827
3.57%, due September 1, 2023.	1,010	1,076
3.64%, due May 1, 2025	1,667	1,761
3.41%, due February 1, 2031	2,993	581
3.40%, due July 1, 2032	782	-
	9,076	6,245
Sub-total	107,676	105,445
Less: current maturities	1,137	964
Total long-term debt	\$ 106,539	\$ 104,481

Payments of principal amounts due during the next five years and thereafter:

<i>In thousands</i>	2012	2013	2014	2015	2016	Thereafter
First Mortgage bonds	\$ 600	\$ 600	\$ 600	\$ 600	\$ 600	\$ 95,600
State revolving fund loans	537	535	556	578	601	6,269
Total payments	\$ 1,137	\$ 1,135	\$ 1,156	\$ 1,178	\$ 1,201	\$ 101,869

Artesian Water Company, Inc.

Notes to Financial Statements

5. Employee Benefit Plans

401(k) Plan

Artesian Resources has a defined contribution 401(k) Salary Deduction Plan, or the 401(k) Plan, which covers substantially all employees of Artesian Water. Under the terms of the 401(k) Plan, the Company contributed 2% of eligible salaries and wages and matches employee contributions up to 6% of gross pay at a rate of 50%. The Company may, at its option, make additional contributions of up to 3% of eligible salaries and wages. No such additional contributions were made in 2011 and 2010. The 401(k) Plan expenses, which include Company contributions and administrative fees, for the years 2011 and 2010, were approximately \$672,000 and \$624,000, respectively.

Supplemental Pension Plan

Effective October 1, 1994, Artesian Water established a Supplemental Pension Plan, or the Supplemental Plan, to provide additional retirement benefits to full-time employees hired prior to April 26, 1994. The Supplemental Plan is a defined contribution plan that enables employees to save for future retiree medical costs, which will be paid by employees. The Supplemental Plan accomplishes this objective by providing additional cash resources to employees upon a termination of employment or retirement, to meet the cost of future medical expenses. Artesian Water has established a contribution based upon each employee's years of service ranging from 2% to 6% of eligible salaries and wages. Artesian Water also provides additional benefits to individuals who were over age 50 as of January 1, 1994. These individuals are referred to as the "Transition Group." Effective November 1, 1994, individuals eligible for the Transition Group had the opportunity to defer compensation to the Supplemental Plan, and to receive a transition matching contribution for 5 years. Each one-dollar of eligible salaries and wages deferred by the Transition Group was matched with three, four, or five dollars by Artesian Water based on the employee's years of service subject to certain limitations under the federal tax rules. Plan expenses, which include Company contributions and administrative fees, for the years 2011 and 2010, were approximately \$264,000 and \$263,000, respectively.

Postretirement Benefit Plan

The Company has a Postretirement Benefit Plan, or the Benefit Plan, which provides medical and life insurance benefits to certain retired employees. Prior to the amendment of the Benefit Plan, substantially all employees could become eligible for these benefits if they reached retirement age while still working for Artesian Water. The amendment excludes any current employees from becoming eligible for these benefits upon retirement.

FASB ASC Topic 715 stipulates that Artesian Water accrue the expected cost of providing postretirement health care and life insurance benefits as employees render the services necessary to earn the benefits. Artesian Water recognizes an offsetting regulatory asset with respect to its

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post retirement liability. This asset is recorded based on the Delaware Public Service Commission, or DEPSC, order, which permits Artesian Water to continue recovery of postretirement health care and life insurance expense on a pay-as-you-go basis for the remaining eligible employees. Further, expense recovery as a percentage of rates is expected to remain generally constant over the initial years, and then decline until the obligation is liquidated. The amounts recognized in consolidated financial statements are determined based on an actuarial basis, which uses assumptions about inflation, mortality, medical trend rates and discount rates. A change in these assumptions could cause actual results to differ from those reported. Amounts charged to expense were approximately \$112,000 and \$111,000 for 2011 and 2010, respectively.

The Company uses December 31 as the measurement date to determine the postretirement benefit obligation. According to our actuarial report, the funded status of our defined benefit postretirement plan was calculated contemplating FASB ASC Topic 715 and the obligation is recorded at that amount. There was no other comprehensive income impact because we record a regulatory asset as provided by FASB ASC Topic 980. Additional disclosures required for our postretirement benefit obligation are presented below.

Benefit Obligations and Funded Status

<i>In thousands</i>	Year Ended December 31,	
	2011	2010
Change in Accumulated Postretirement Benefit Obligation		
Accumulated Postretirement Benefit Obligation at the		
Beginning of the Year	\$ 678	\$ 785
Interest Cost	34	44
Actuarial (Gain) or Loss	123	(40)
Benefits Paid	(117)	(115)
Plan Participant's Contributions	5	4
Accumulated Postretirement Benefit Obligation at the		
End of the Year	723	678
Change in Plan Assets		
Fair Value of Plan Assets at the Beginning of the Year	-	-
Benefits Paid	(117)	(115)
Employer Contributions	112	111
Plan Participant's Contributions	5	4
Fair Value of Assets at the End of the Year	-	-
Net Amount Recognized		
Funded Status	(723)	(678)
Unrecognized Transition Obligation Asset	17	26
Unrecognized Net Gain or Loss	139	15
Net Amount Recognized:	(567)	(637)
Amounts Recognized in the Balance Sheets		
Accrued Benefit Liability-Current	(112)	(112)
Accrued Benefit Liability-Noncurrent	(455)	(525)
Net Amount Recognized	\$ (567)	\$ (637)

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<i>In thousands</i>	Year Ended December 31,	
	2011	2010
Weighted Average Assumptions at the End of the Year		
Discount Rate	4.50%	5.50%
Assumed Health Care Cost Trend Rates		
Health Care Cost Trend Rate Assumed for Next Year	7.00%	7.00%
Ultimate Rate	3.50%	4.50%
Year that the Ultimate Rate is Reached	2015	2014
Impact of One Percentage Point in Assumed Health Care Cost Trend Rates	Increase	Decrease
Effect on Service Cost & Interest Cost	\$ 1	\$ (1)
Effect on Postretirement Benefit Obligation	\$ 27	\$ (25)

Contributions

Artesian Water expects to contribute \$111,500 to its postretirement benefit plan in 2012. The following table represents the approximate annual benefits expected to be paid for the years ended December 31:

	(In thousands) Other Benefits
2012	\$ 112
2013	105
2014	96
2015	87
2016	77
2017 through 2020	250
	\$ 727

6. Commitments and Contingencies

Leases

In October 1997, Artesian Water entered into a 33-year operating lease for a parcel of land with improvements located in South Bethany, a municipality in Sussex County, Delaware. The annual lease payments increase each year by the most recent increase in the Consumer Price Index for Urban Workers, CPI-U, as published by the U.S. Department of Labor, Bureau of Labor Statistics. At each eleventh year of the lease term, the annual lease payment shall be determined based on the fair market value of the parcel of land. Rental payments for 2011 and 2010 were \$15,300 and \$12,700, respectively. The future minimum rental payment as disclosed in the following table is

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calculated using CPI-U as of October 31, 2011 as well as any adjustments for appraisals conducted to determine the fair market value of the parcel of land.

In October 2006, Artesian Water entered into a 3-year contract for office space located in Sussex County, Delaware. In October 2009 the contract term was extended for an additional year and therefore ended in October 2010. Rent payments for 2010 were \$40,000.

During September 2007, Artesian Water entered into a 3-year contract for office space located in New Castle County, Delaware. The contract ended in August 2010. This location was used as general office space while the Artesian Water main office space was being renovated. Rent payments during 2010 were \$53,000.

In November 2010, Artesian Water entered into a 5-year contract with Artesian Development Corporation, a subsidiary wholly owned by Artesian Resources, for office space located in Sussex County, Delaware. Rental payments for 2011 and 2010 were \$110,000 and \$15,000, respectively.

Future minimum annual rental payments related to operating leases for the years subsequent to 2011 are as follows:

	<i>(In thousands)</i>
2012	\$ 135
2013	136
2014	137
2015	117
2016	18
2017 through 2030	295
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	\$ 838

Interconnections

Artesian Water has one water service interconnection agreement with a neighboring utility, Chester Water Authority, which requires minimum annual purchases. Rates charged under this agreement are subject to change. Effective August 1, 1997, Artesian Water renegotiated the contract with the Chester Water Authority to, among other things, reduce the minimum purchase requirements from 1,459 million gallons to 1,095 million gallons annually, calculated as 3 million gallons per day times the number of calendar days in a year. The agreement is extended through the year 2021.

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The minimum annual purchase commitments for all interconnection agreements for 2012 through 2016 and the aggregate total for the years 2017 through 2021, calculated at the noticed rates, are as follows:

	(In thousands)
2012	\$ 3,791
2013	3,780
2014	3,780
2015	3,780
2016	3,791
2017 through 2021	18,913
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	\$ 37,835

Expenses for purchased water were approximately \$3,809,000 and \$3,636,000 for the years ended December 31, 2011 and 2010, respectively.

Other Commitments

In 2005, Artesian Water entered into a 6-year agreement with Utility Service Co., Inc. to clean and paint tanks from 2006 to 2011 for \$1.9 million. The tank painting expense for 2011 and 2010 was \$344,000, \$364,000, respectively. In 2011, Artesian Water entered into a 2-year agreement with Southern Corrosion Inc. to clean and paint tanks in 2012 and 2013. Pursuant to the 2-year agreement, the expenditure committed for the years 2012 through 2013 is \$623,000.

Budgeted mandatory utility plant expenditures, due to planned governmental highway projects, which require the relocation of Artesian Water's water service mains, expected to be incurred in 2012 through 2016 are as follows:

	(In thousands)
2012	\$ 1,655
2013	950
2014	525
2015	50
2016	550
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	\$ 3,730

The exact timing and extent of these relocation projects is controlled primarily by the Delaware Department of Transportation.

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Litigation

Artesian Resources and its subsidiaries are subject to legal proceedings in the ordinary course of business. Any amounts from such legal proceedings that are probable and reasonably estimable are reflected in the financial statements.

On December 22, 2010, Artesian Water filed a complaint in the United States District Court for the Eastern District of Pennsylvania against Chester Water Authority claiming breach of contract, unjust enrichment and requesting declaratory judgment in relation to an agreement by Chester Water to supply bulk water supplies to Artesian Water. On February 11, 2011, Artesian Water received an answer and counterclaim from Chester Water Authority denying Artesian Water's claims and allegations, asserting a counterclaim for breach of contract and seeking monetary damages, related costs and attorneys' fees. Although Artesian Water intends to pursue its claims and defense in the action vigorously, there can be no assurances that it will prevail on any of the claims in the action, or, if it does prevail on one or more claims, of the amount or nature of recovery that may be awarded.

Related to the ongoing litigation with Chester Water Authority, we have approximately \$1.1 million and \$0.4 million of accrued expenses recorded on our Balance Sheets as of December 31, 2011 and December 31, 2010, respectively. These accrued expenses represent the disputed portion of Chester Water Authority's rate increases and have been withheld from payments to Chester Water Authority pending the outcome of the litigation.

7. Related Party Transactions

Artesian Resources Corporation operates as the parent holding company of eight wholly-owned subsidiaries offering water, wastewater and engineering services on the Delmarva Peninsula. The subsidiaries include: Artesian Water, Artesian Water Pennsylvania, Inc., Artesian Water Maryland, Inc., Artesian Wastewater Management, Inc., Artesian Wastewater Maryland, Inc., each a regulated public utility, and three non-regulated subsidiaries; Artesian Utility Development, Inc., Artesian Development Corporation, and Artesian Consulting Engineers. Artesian Water has entered into transactions in the normal course of business with these subsidiaries.

For the year ended December 31, 2011, Artesian Water had an intercompany loan receivable balance due from Artesian Resources Corporation of \$10.9 million at an average interest rate of 1.3%. The corresponding interest income for the year ended December 31, 2011 was \$33,000. For the year ended December 31, 2010, Artesian Water had an intercompany loan payable balance due to Artesian Resources Corporation of \$1.7 million at an average interest rate of 1.7%. The corresponding interest expense for the year ended December 31, 2010 was \$17,000. Artesian Water provides various administrative services to all other subsidiaries, and costs to perform these services are allocated accordingly, primarily based on a percentage of sales of each subsidiary. Artesian Water also has intercompany transactions for temporary federal income tax attributes.

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For the year ended December 31, 2011, Artesian Water had an intercompany payable balance to the other subsidiaries of approximately \$234,000. For the year ended December 31, 2010 Artesian Water had an intercompany receivable balance from the other subsidiaries of approximately \$258,000. For the years ended December 31, 2011 and December 31, 2010, Artesian Water had intercompany water sales of approximately \$364,000 and \$70,000, respectively, from Artesian Water Maryland, Inc. for an interconnection between Delaware and Maryland. For the years ended 2011 and 2010, Artesian Water had intercompany rent expense of approximately \$110,000 and \$15,000, respectively, to Artesian Development Corporation for office space located in Sussex County, Delaware.

8. Rate Proceedings

On April 11, 2011, Artesian Water filed a request with the DEPSC to implement new rates to meet a requested increase in revenue of 19.45%, or approximately \$10.9 million, on an annualized basis. The new rates are designed to support Artesian Water's ongoing capital improvement program and to cover increased costs of operations, including chemicals and fuel, electricity, taxes, labor and benefits. Artesian Water's last request to implement new rates was filed in April 2008. As permitted by law, on June 10, 2011, we placed temporary rates into effect designed to generate an increase in annual operating revenue of approximately 4.45%, or \$2.5 million on an annualized basis, until new rates were approved by the DEPSC. Also as permitted by law, on November 11, 2011, we placed into effect a second step of temporary rates designed to generate an additional increase in annual operating revenue of approximately 6.68%, or \$3.8 million on an annualized basis, until new rates were approved by the DEPSC.

Artesian Water, the DEPSC, and the Division of the Public Advocate entered into an agreement to settle Artesian Water's April 2011 application for an increase in rates. PSC Order No. 8097, issued on January 31, 2012, approved the settlement agreement, authorizing a permanent rate increase in revenue of approximately 11.13%, or \$6.25 million on an annualized basis. Since the permanent rate increase did not exceed amounts previously collected under previously approved temporary increases in rates, Artesian Water was not required to refund any amounts to its customers. The approved permanent rate increase is effective as of January 1, 2012. The settlement also authorizes a return on equity of 10%. Additionally, effective January 1, 2012, the settlement permits a tariff change that includes the use of a seasonal connection charge as well as a new approach for presenting the cost of retired property and ratemaking treatment for salvage costs to be recovered in rates. Currently, when depreciable units of utility plant are retired, the cost of retired property, together with any cost associated with retirement less any salvage value or proceeds received, is charged to accumulated depreciation. The settlement authorizes that effective January 1, 2012, any cost associated with retirement less any salvage value or proceeds received will be charged to a regulated retirement liability. This new approach will result in an approximately \$1.2 million reclassification of utility plant to deferred credits and other liabilities on our Consolidated Balance Sheet in our fiscal year 2012. The settlement also authorizes Artesian Water to change from quarterly to monthly billing. Implementation of the change to

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monthly billing is expected to take place during the second quarter of 2012.

Delaware law permits water utilities to put into effect, on a semi-annual basis, increases related to specific types of distribution system improvements through a Distribution System Improvement Charge, or DSIC. This charge may be implemented by water utilities between general rate increase applications that normally recognize changes in a water utility's overall financial position. The DSIC approval process is less costly when compared to the approval process for general rate increase requests. The DSIC rate applied between base rate filings is capped at 7.5% of the amount billed to customers under otherwise applicable rates and charges, and the DSIC rate increase applied cannot exceed 5% within any 12-month period. During 2010, Artesian Water filed two applications with the DEPSC for approval to collect a 0.34% increase and 0.68% increase during the first and second half of the year, respectively. These increases recover the costs of eligible revenue producing improvements made since the last rate increase in 2008, and were calculated to generate approximately \$286,000 in revenue annually. In November 2010, we filed an application with the DEPSC for approval to increase the DSIC rate to 1.47% effective January 1, 2011. The DEPSC approved the DSIC effective January 1, 2010, July 1, 2010 and January 1, 2011, subject to audit at a later date. For the year ended December 31, 2011, we earned approximately \$346,000 in DSIC revenue. For the year ended December 31, 2010, we earned approximately \$288,000 in DSIC revenue.

9. Geographic Concentration of Customers

The Company provides water utility service to customers within its established service territory in all three counties of Delaware, pursuant to rates filed with and approved by the DEPSC. As of December 31, 2011, the Company was serving approximately 78,600 customers.

10. Common Stock Offering

On July 20, 2011, Artesian Resources completed the sale of 804,290 shares of its Class A Non-Voting Common Stock. The net proceeds (after deducting underwriting discounts and commissions and offering expenses) of approximately \$14.1 million were used to fund a paid-in capital contribution in the same amount to Artesian Water. Artesian Water used the paid-in capital contribution to repay short-term borrowings (including borrowings incurred under our line of credit with Citizens Bank that is available to all of our subsidiaries) incurred primarily to finance expenses associated with its construction program, including investment in utility plant and equipment, and to fund capital expenditures and other general corporate purposes.

On August 15, 2011, Artesian Resources completed the sale of an additional 84,000 shares of its Class A Non-Voting Common Stock, in accordance with the option granted to the underwriters to cover over-allotments associated with our July 2011 stock offering. The net proceeds of approximately \$1.5 million were used to fund a paid-in capital contribution in the same amount to Artesian Water as noted above.

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